

## **DECISION OF MUNICIPAL TAX HEARING OFFICER**

Decision Date: July 29, 2014

Decision: MTHO # 826

***Taxpayer: Engineer Contractor***

Tax Collector: City of Flagstaff

Hearing Date: None

### **DISCUSSION**

#### **Introduction**

On February 21, 2014, a letter of protest was filed by ***Engineer Contractor*** (“Taxpayer”) of a tax refund denial made by the City of Flagstaff (“City”). This matter was classified as a hearing. Subsequently, at the request of Taxpayer, this matter was reclassified as a redetermination. After submission of all memoranda by the parties, the Municipal Tax Hearing Officer (“Hearing Officer”) closed the record on July 24, 2014 and indicated a written decision would be issued on or before September 5, 2014.

### **DECISION**

In 2011, Taxpayer completed construction of a cast in place 16 foot diameter storm water drainage culvert at ***ABCD Street*** in the City. Taxpayer paid construction contracting taxes related to the project to the City. Following completion of the culvert project, the Arizona Department of Revenue (“DOR”) conducted a joint audit of Taxpayer related to both state and local transaction privilege taxes.

As a result of the DOR audit, Taxpayer filed a refund request with the City in the amount of \$9,960.82. Taxpayer indicated the over payment was related to taxes erroneously paid for materials and services falling within the tax deduction related to Arizona Revised Statutes Sections 42-5061(B)(6) (“Section 5061”) and 42-5159(B)(6) (“Section 5159”). On February 10, 2014, the City denied the Taxpayer’s request for a refund. Subsequently, Taxpayer timely protested the City’s denial.

During the audit period, Taxpayer had purchased sand, grout, and other materials used to construct a cast in place concrete storm water culvert. In its refund request, Taxpayer had requested a tax exemption for the purchase of pipes and valves 4 inches or larger in diameter.

City Code Section 3-05-004-415 (“Section 415”) imposes a tax on the gross income from construction contracting. Subsection (b)(3) of Section 415 provides for an exemption for gross income attributable to the purchase of machinery, equipment, or other tangible personal property that is exempt from privilege tax under City Code Section 3-05-004-465 (“Section 465”), subsection (g). Subsection (g) of Section 465 exempts sales of income producing capital equipment. City Code Section 3-05-004-110 (“Section 110”) defines “income-producing capital equipment to include pipes or valves four inches in diameter or larger used to transmit water. City Code Section 3-05-004-360 (“Section 360”) provides that all exemptions are conditional upon adequate proof and documentation being provided by the taxpayer.

There was no dispute that Taxpayer purchased concrete mix, grout mix, and sand to construct a concrete culvert in excess of four inches to transmit storm water. While Taxpayer relied upon Sections 5061 and 5159 of the Arizona Revised Statutes, the Model City Tax Code is controlling in this matter. We also note there is very little difference between the cited State Statutes and the cited Model Code Sections. Taxpayer also relied upon Arizona Transaction Privilege Tax Ruling TPR 02-2. We note that TPR 02-2 addresses the use of the four inch or larger diameter pipes. Since we have concluded the concrete culvert that was constructed was used to transmit storm water, we can see no conflict with TPR 02-2 in our analysis.

In our review of the claimed exemption by Taxpayer for the purchase of pipes or valves of four inches or larger in diameter used to transmit water, we are mindful that Taxpayer has the burden of proof pursuant to Section 360 for any claimed exemption. We also note that our review of the language is based upon the plain and ordinary meaning of the language of the Code. In this case, we are helped by the definition of “culvert” provided by Taxpayer. That definition indicates a “culvert” is a structure that allows water to flow under a road. It goes on to indicate a culvert may be made from a pipe, reinforced concrete or other material. From that definition, we can conclude that a pipe can be used as a culvert but a culvert can be something other than a pipe. The language of Section 110 only refers to pipes or valves and not the broader term of culvert. Certainly, the drafters could have used the broader term for culverts if that was their intent. Since that wasn’t done, we conclude the exemption was only for pipes. Accordingly, we conclude Taxpayer has failed to meet its burden of proof for the claimed exemption. Based on all the above, we conclude that Taxpayer’s protest should be denied consistent with the Discussion, Findings, and Conclusions, herein.

## **FINDINGS OF FACT**

1. In 2011, Taxpayer completed construction of a cast in place 16 foot diameter storm water drainage culvert at *ABCD Street* in the City.
2. Following completion of the culvert project, the DOR conducted a joint audit of Taxpayer related to both state and local transaction privilege taxes.
3. As a result of the DOR audit, Taxpayer filed a refund request with the City in the amount of \$9,960.82.
4. Taxpayer indicated the over payment was related to taxes erroneously paid for materials and services falling within the tax deduction related to Sections 5061 and 5159.
5. On February 10, 2014, the City denied Taxpayer's refund request.
6. On February 21, 2014, Taxpayer filed a protest of the City's denial.
7. Taxpayer requested this matter be reclassified as a redetermination without a hearing.
8. During the audit period, Taxpayer had purchased sand, grout, and other materials used to construct a cast in place concrete storm water culvert.
9. Taxpayer had requested a tax exemption for the purchase of pipes and valves 4 inches or larger in diameter.
10. A culvert is a structure that allows water to flow under a road.
11. A culvert may be made from a pipe, reinforced concrete or other materials.

## **CONCLUSIONS OF LAW**

1. Pursuant to ARS Section 42-6056, the Municipal Tax Hearing Officer is to hear all reviews of petitions for hearing or redetermination under the Model City Tax Code.

2. Section 415 imposes a tax on the gross income from the business activity of construction contracting.
3. Subsection (b)(3) of Section 415 provides for an exemption for gross income attributable to the purchase of machinery, equipment, or other tangible personal property that is exempt from privilege tax under Section 465, subsection g.
4. Subsection g of Section 465 exempts sales of income-producing capital equipment.
5. Section 110 defines income-producing capital equipment to include pipes or valves four inches in diameter or larger used to transmit water.
6. Section 360 provides that all exemptions are conditional upon adequate proof and documentation being provided by the taxpayer.
7. TPR 02-2 addresses the use of the four inch or larger diameter pipes.
8. Our review of the language of “four inch or larger diameter pipes” is based on the plain and ordinary meaning of the language.
9. Based on the definition of “culvert”, we conclude that a pipe can be used as a culvert but a culvert can be something other than a pipe.
10. The language of Section 110 only refers to pipes or valves and not the broader term of culvert.
11. The drafters of Section 110 could have used the broader term for culverts if that had been their intent.
12. The exemption set forth in subsection (b)(3) of Section 415 was only for pipes and not culverts.
13. Taxpayer failed to meet its burden of proof for the claimed exemption pursuant to Section 360.
14. Based on all the above, Taxpayer’s protest should be denied, consistent with the Discussion, Conclusions, and Findings, herein.
15. The parties have timely rights of appeal to the Arizona Tax Court pursuant to Model City Tax Code Section-575.

**ORDER**

It is therefore ordered that the February 21, 2014 protest by *Engineer Contractor* of a denial made by the City of Flagstaff of a request for a refund is hereby denied, consistent with the Discussion, Findings, and Conclusions, herein.

It is further ordered that this Decision is effective immediately.

Municipal Tax Hearing Officer